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TREASURY PLEASE PASS TO OCC/AMCMAHON
TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF
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SUBJECT: New Taiwan Foreign Currency Bond Market

REF: Taipei 2695

SUMMARY

1. (SBU) Taiwan has established a foreign currency bond market and expects the first bond listings in October. The move is another in a series of measures designed to better utilize Taiwan's surplus capital. However, restrictions such as limits on PRC investment and the lack of incentives will limit the bond market's appeal and utility. End summary.

Bonds Denominated in Foreign Currency

2. (U) In late August, the Taiwan Securities and Futures Bureau (SFB) announced rules for a new foreign currency bond market that will allow any company listed on the 19 foreign stock markets recognized by the FSB, foreign governments, and international organizations to list bonds denominated in U.S. dollars, Euros, Japanese yen and other currencies. Local and foreign investors, except those from China, may trade bonds listed on the new market. This will help soak up and utilize Taiwan's huge capital surplus (reftel).

3. (SBU) Taiwan's Over-the-Counter (OTC) Center, which will operate the new market, says Deutsche Bank plans to issue US\$300-500 million of bonds in October and several other foreign companies have expressed interest. Over 20 underwriters have applied to the Foreign Exchange Department under Taiwan's Central Bank of China for foreign currency bond underwriting licenses. The OTC Center estimates the total value of bonds listed will reach NT\$100 billion (US\$3.1 billion) by the end of 2009.

Securities Transaction Taxes Waived

¶4. (U) The securities transaction tax will be waived for transactions in this new market, as it is in the NT\$ bond market. Individuals will be exempt from income tax on interest earned on foreign currency bonds issued by offshore companies because Taiwan's tax law exempts individual income earned from overseas sources. However, corporate entities must pay income tax on overseas income. Both individuals and corporate entities are subject to income tax on interest earned from bonds issued by domestic companies.

¶5. (SBU) Taiwan prohibits firms listed on the Taiwan Stock Exchange from investing more than 40% of their net worth in China. This same restriction will also apply to companies listing on the foreign currency bond market. Taiwan has also relatively strict listing requirements, such as a minimum credit rating, that foreign bond markets do not have. These restrictions will dampen the enthusiasm of multinational corporations for issuing and listing bonds in Taiwan, even though listing and underwriting costs in Taiwan are less than in other bond markets.

Bond Markets Very Competitive

¶6. (SBU) The Chief Financial Officer of a major U.S. company told AIT bond markets in East Asia are very competitive. She said it was not uncommon for regulators to require use of some local financing in major investment projects. Without any requirement to use local financing, she said, her company would continue to rely on cheaper capital from Japan's bond markets for its projects in Taiwan.

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¶7. (SBU) Although the appeal to companies may be limited, Taiwan's new bond market may be attractive to local individuals because the trading unit is only US\$10,000 and individuals are exempt from Taiwan income tax on interest earnings.

Comment

¶8. (SBU) Taiwan authorities need to find a way to utilize Taiwan's surplus capital, but are stymied by political factions opposed to facilitating investment in China. While the recent establishment of a foreign currency bond market is a small step forward in internationalizing Taiwan's financial markets, the current regulations limit its appeal.

Young